MULTIMEDIA UNIVERSITY

STUDENT IDENTIFICATION NO

MULTIMEDIA UNIVERSITY

FINAL EXAMINATION

TRIMESTER 3, 2018/2019 SESSION

BAC2684 – FINANCIAL STATEMENT ANALYSIS

(All Section / Groups)

29 MAY 2019
2.30 PM – 5.30 PM
(3 Hours)

INSTRUCTIONS TO STUDENT

1. This question paper consists of 6 pages excluding cover page with 4 Questions only.
2. Attempt ALL questions. The distribution of the marks for each question is given.
3. Please write all your answers in the Answer Booklet provided

QUESTION 1

(a) Briefly explain the primary and secondary desirable qualities of accounting information required to evaluate the strengths and weaknesses of accounting and its relevance to effective analysis and decision making.

(6 marks)

(b) Explain **TWO (2)** factors that give rise to the superiority of accrual accounting over cash accounting.

(5 marks)

(c) On 1 April 2018, MAJU Berhad expanded its operating capacity of its manufacturing plants. However, they lack funds to acquire special machine to the plant costing of RM350,000. CFO, recommended MAJU Berhad to enter into a lease agreement to lease a special plant machine from Leasing Company. Lease terms stipulated four (4) annual payments in advance of RM100,000 each commencing 1 April 2018. The plant machine would have a useful life of 4 years and would be scrapped at the end of the period. CFO believed that the lease to be an operating lease, commented that the agreement would improve the company's return on capital employed (compared to outright purchase of plant machine).

Required:

(i) Identify the types of lease and describe the **FOUR (4)** criteria for classifying leases by a lessee.

(4 marks)

(ii) Prepare extracts of MAJU Berhad's income statement and Statement of Financial Position for the year ended 30 September 2018 in respect of the rental agreement assuming:

(a) It is an operating lease

(2 marks)

(b) It is a capital (finance) lease (use an implicit interest rate of 10% per annum).

(8 marks)

Total 25 marks

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QUESTION 2

NBW Berhad is a public listed company. The following are the financial statements of NBW Berhad

Statement of Financial Position as at 31 March:

	2018		2017	
	RM'000	RM'000	RM'000	RM'000
Assets				
Non-current assets		2,880		1,860
Investment property		120		400
		3,000		2,260
Current assets				
Inventory	1,210		810	
Trade receivables	780		540	
Income tax asset	-		50	
Bank	10	2,000	-	1,400
Total Assets		5,000		3,660
Equity and liabilities				
Equity shares of 20sen each		1,000		600
Share premium	600		-	
Revaluation reserve	150		50	
Retained earnings	1,440	2,190	1,310	1,360
		3,190		1,960
Non-current liabilities				
6% loan notes	-		400	
Deferred tax	50	50	30	430
Current liabilities				
Trade payables	1,410		1,050	
Bank overdraft	-		120	
Warranty provision	200		100	
Current tax payable	150	1,760	-	1,270
Total equity and liabilities		5,000		3,660

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Statement of comprehensive income for the year ended 31 March 2018:

	RM'000
Revenue	5,740
Cost of sales	(4,840)
Gross profit	900
Income from and gains on investment property	60
Distribution costs	(120)
Administrative expenses	(350)
Interest cost	(50)
Profit before tax	440
Income tax expense	(160)
Profit for the year	280

Additional information:

- Term of sales are net 30 days
- One year equals to 360 days

Required:

(i) Compute the following ratio for year 2018

(a) Working capital
(b) Current ratio
(c) Acid-test ratio
(d) Accounts receivables turnover
(e) Collection period of receivables
(f) Inventory turnover
(g) Days to sell inventories
(h) Debt-to-equity ratio
(i) Times related earned
(j) Working capital turnover

(20 marks)

(ii) In assessing liquidity, it is necessary to measure the quality of its liquidity. Based on the above assessment in (a), how can analysis and use of other related measures (other than the current ratio) enhance the evaluation of liquidity, including its quality?

(5 Marks)

Total 25 marks

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QUESTION 3

(a) Statement of cash flows provides information on cash inflows and outflows for the period. List **FIVE (5)** insights that the statement of cash flows can provide to our analysis.

(5 marks)

(b) Malware Corporation product sales have increased dramatically. However Management noted that despite increasing profits, the cash balance has declined and are forced to nearly double its debt financing in the current year. The management is now seeking an advised from you as CFO as to the specific causes of the cash deficiency and how to remedy the situation.

The following are the Statement of Financial Position balances of Malware Corporation for Year 2017 and 2018 (RM thousand);

MALWARE CORPORATION
Statement of Financial Position
December 31,

(RM'000)	2018		2017	
Assets				
Cash		500		640
Account Receivables, net		860		550
Inventories		935		790
Prepaid expenses		25		-
Total current assets		2,320		1,980
Patents	140			
Less Accumulated amortization	(10)	130		-
Plant and equipment	2,650		1,950	
Less Accumulated depreciation	(600)	2,050	(510)	1,440
Other assets	200		175	
Less Accumulated depreciation	(30)	170	(25)	150
Total Assets		4,670		3,570
Liabilities and Equity				
Accounts payable		630		600
Deferred income tax		57		45
Other current liabilities		85		78
Total current liabilities		772		723
Long-term debt		1,650		850
Ordinary Share, RM1 par		2,000		1,800
Retained Earnings		248		197
Total liabilities and equity		4,670		3,570

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In addition, the following information is available;

1. Net income in Year 2018 is RM160,000 and for Year 2017 is RM130,000

2. Cash dividends paid during Year 2018 are RM109,000 and during Year 2017 are RM100,000

3. Depreciation expense charged to income during Year 2018 is RM95,000 and the provision for bad debts (expense) is RM40,000. Expenses include cash payments of RM28,000 in interest costs and RM70,000 in income taxes.

4. During Year 2018 the company purchases patents for RM140.000 in cash. Amortization of patents during the year amounts to RM10,000.

5. Deferred income tax for Year 2018 amounts to RM12,000 and for Year 2017 it amounts to RM15.000.

Required:

(i) Prepare a Statement of Cash Flows using the indirect method as at Dec 31, 2018.
(11 marks)

(ii) Explain the discrepancy between net income and cash flows from operations
(3 marks)

(iii) Describe **THREE (3)** options for management to remedy the cash deficiency.
(6 marks)

Total 25 marks

QUESTION 4

(a) General Electronic Corporation (GEC), a successful and high growth company, consistently experiences a favorable difference between the rate of return on its assets and the interest rate paid on borrowed funds.

Explain why this company should increase its debts to the 90% level of total capitalization and thereby minimize any need for equity financing.
(6 marks)

(b) In estimating the value of common stock, the amount of EPS is considered an important element. Explain why EPS is important in the valuation of common stock.
(5 marks)

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(c) Selected income statement and balance sheet data from MMC Corp. for Years 5 and Year 9 are reported below:

MMC Corp.
Year 9 Selected Financial Data (RM million)

	Year 5	Year 9
Income Statement Data	RM	RM
Revenues	542	979
Operating income	35	68
Interest expense	7	0
Pretax income	28	68
Income taxes	14	34
Net income	14	34
Statement of Financial Position		
Long-term operating assets	52	63
Working capital	123	157
Total liabilities	50	0
Total shareholders' equity	125	220

Required:

(i) Calculate the return on common equity (ROCE) and disaggregate ROCE for Years 5 and 9 using end-of-year values for computations requiring an average (assume fixed assets and working capital are operating and a 50% tax rate)

(12 marks)

(ii) Comment on MMC Corp's use of leverage.

(2 mark)

Total 25 marks

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